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C O N F I D E N T I A L SECTION 01 OF 03 LA PAZ 001024

SIPDIS

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TAGS: ECON PGOV PREL ENRG EPET EINV BL
SUBJECT: BOLIVIAN MAY DAY GAS NATIONALIZATIONS

REF: LA PAZ 614

Classified By: EcoPol Chief Mike Hammer for reasons 1.4 (b) and (d).

Summary

¶1. (C) President Morales announced on May 1 the next step in "consolidating the nationalization" of the hydrocarbon sector begun two years ago. In a series of decrees, the government mandated the acquisition of a 50 plus 1 percent shares of the three capitalized companies of Andina, Chaco, and Transredes. While a fourth, the Bolivian Hydrocarbon Logistical Company (CLHB), will be 100 percent owned by the government. Only Andina, controlled by the Spanish company Repsol, has formally signed an agreement. The day following the announcements, uncertainty is the rule across the sector and further negotiations appear likely on the sticking point of operational control at all three of the mixed ownership companies. Meanwhile, executives from CLHB are calling the move an outright expropriation. Ultimately, as "observers" from the Bolivian state oil company (YPFB) show up at company offices and police guard the exits, the only sure result of the May 1 announcements is greater uncertainty in the industry and more delays in making needed investments for increased production and infrastructure improvements. End summary.

Andina (Repsol - Spanish)

¶2. (C) The agreement to reach 50 plus 1 ownership in Andina was announced in a televised ceremony preceding President Morales' formal May 1 speech. The company agreed to sell a little over one percent of its stock, valued at $6.2 million. The agreement establishes a "mixed commission" for administrative control of the company, but anticipates complete YPFB control in the future. In meetings with Ecopol officer, the Repsol Director of the Andina Unit, Roberto

Domingues, said that if the government insisted in making Repsol a passive partner in Andina, they would demand that they take the whole company. Considering this position, it is likely that Repsol ultimately intends to allow Andina to be fully taken over by the YPFB. Rumor has a timetable being set for between 12 to 16 months.

¶3. (C) A future full take over of Andina makes sense. As reported in the papers, Andina represents less that 1 percent of Repsol's worldwide activities. Moreover, Andina's share of Bolivian gas production is smaller than direct Repsol operations; Repsol produced approximately 25% of Bolivian gas in 2007, while Andina's share was only 8% of the total. Given reported Spanish government pressure to "make a deal" with the Bolivian government, this is an understandable move both to placate the political powers in both countries and to ensure that profitable operations in Bolivia for Repsol continue well into the future.

¶4. (C) Both Andina and Chaco are the companies that most benefited from legal changes in the sector made in May 2005. Before that date, these companies supplied a large part of the domestic market (at highly subsidized prices). However, the government changed the formula and now each company operating large gas fields must supply the domestic market proportionally to the percentage of total gas pumped. For example, the biggest loser in the redesign was Petrobras. Before the legal changes, Petrobras, which produces about half of all gas in Bolivia, had no obligation to the domestic market; now Petrobras is obligated to supply over half of the

domestic market. (Note: Small fields are except from the arrangement. As a result, American owned Vintage, which operates a small field, is allowed to export all of its production to Argentina. Petrobras has to supply 3.5 million cubic meters of gas per day (Mm3/d) toward fulfilling a domestic demand which varies between 5 Mm3/d and 6Mm3/d. End note).

¶5. (C) Repsol is enthusiastic about investment opportunities in Bolivia. In March, Dominguez cited the lack of any strong union (as opposed to Argentina), easy access to the gas, and good tariffs in the export contracts to Brazil and Argentina. Moreover, Repsol is exploring the possibility of connecting its new gas discovery in the state of Chuquisaca with the mega-field of Margarita. According to Dominguez, the company was anticipating investing a total of some $1 billion by 2011. The biggest obstacle to these investments was incompetence in YPFB (Reftel); incompetence that may now have a greater say in Andina's administration over the coming year.

Chaco (Pan American - Argentina)

¶6. (C) As with Andina, selling the government a majority share in Chaco was never the bone of contention; operational control was and is the key. But unlike Andina, where the other interests of the parent company in Bolivia played a role, Argentina's Pan American Energy have no other interests in Bolivia. While the government has decreed the sale of 50 plus 1 percent of shares in the company, the situation is far from settled. Without operational control, Chaco (and Transredes) view the remaining 49 percent of the company as severely discounted. Acceptance of passive ownership does not appear to be an option and takeover of 51 percent and operational control would amount to complete nationalization. Despite Evo's May 1 pronouncement, operational control of the company is not yet defined. According to the British DCM, Steve Townsend, the decree only defines the amount of shares purchased and the price. According to Jana Drakic, Chaco Vice-president, following all night negotiations on April 30th, executives from Pan American Energy went back to Buenos Aires the morning of May 1, but negotiations are

likely to be restarted next week. Bolivian "nationalization" is still a work in progress, but three YPFB employees did report to the Chaco offices on May 2 to observe operations.

Transredes
(Ashmore Energy, based in Houston and owned by Ashmore Investments in London and Shell, Holland)

¶7. (C) The government had the farthest to come to gain a 51 percent stake in Transredes, but the shares of several minority stakeholders have been obtained (some 16 percent of the company) and now ownership appears to be YPFB (50%), Ashmore Energy (25%), and Shell (25%). While the sale of 50 plus 1 percent has been mandated by decree, details associated with the golden one percent will still need to be negotiated. According to Jose Gordillo, Vice President of Sales and Regulations at Transredes, the principal shareholders have three options: 1) become passive shareholders; 2) sell all remaining shares; or 3) go to international arbitration.

¶8. (C) In reopening today, Transredes is trying to go about business as normal. There are between 10 to 15 policeman guarding the exit (ostensibly to make sure nothing is removed) and some six YPFB observers reported to "work". However, in the weeks ahead many fundamental questions will

need to be answered for the principle hydrocarbon transport operator in Bolivia. For example, change of control clauses may well kick in for banks and insurance companies. Most of the funding for current pipeline projects are being financed by the Inter American Development Bank (IDB) and the Andean Development Corporation (CAF), which are likely to continue loans even if the government is the principal owner (at least for projects currently underway). Insurance may be a different story; while insuring pipelines for a private company with a proven track record is one thing, insuring the operations of YPFB is entirely different. Moreover, it is unlikely that Shell will be willing to continue funding needed projects to expand the network. This includes a new pipeline underway that is vital to ensure adequate electricity for La Paz in the winter of 2009 (Note: The new pipeline will connect a line which ends in Carrasco, Cochabamba to the city of Cochabamba. End note). For now, everything is on hold.

CLHB (Outright German and Peruvian Ownership)

¶9. (C) According to the Financial Manager of CLHB, the company has been expropriated. YPFB personal are in the building and the nationalization decree states that there will be a 30 day period to work out the details. YPFB will assume an $8 million debt of the company and pay the owners $12 million for outright ownership. The shareholders began negotiations with the government valuing the firm at $45 million and even their final offer of $40 million is more than double the government's decree. By all accounts negotiations were intense and acrimonious. On April 30, both the German and Peruvian Embassies confirmed that an oral agreement had been reached for the sale of 51 percent of the firm. Officials were caught by surprise by the May 1 announcement and the Bolivian ambassador in Germany is being convoked to make sure that Bolivia is aware of possible consequences (including the cut-off of all aid programs).

Comment

¶10. (C) The "nationalization" of the hydrocarbons sector has been Morales' most popular initiative in his two-plus

years in office. The May 1 decrees likely are an attempt to reenergize his base leading into the May 4 vote on autonomy in Santa Cruz. The economic uncertainty these actions will create appear secondary to the short-sighted political agenda of the current administration. There will also be a diplomatic cost to relations with Europe which, at the moment, does not seem to be a priority for the government. Bolivia may learn just how peeved the Europeans are at the EU/LAC summit in Lima on May 14.

GOLDBERG